In the Supreme Court of the United States

OCTOBER TERM, 1975

No. 74-1376

CITIES SERVICE COMPANY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE UNITED STATES

This case challenges other aspects of the court of appeals' decision which we are challenging in our petition for a writ of certiorari in No. 75-9, *United States* v. *Cities Service Company*. The issue presented in our petition is whether the court of appeals erred in holding that respondent's issuance of debentures in exchange for its outstanding preferred stock, pursuant to an order of the Securities and Exchange Commission, gave rise to amortizable bond discount equal to the difference between the face amount of the debentures ($115,246,950) and their market value at issuance (approximately $106,000,000). As we there explain, under this Court's decision in *Commissioner* v. *National Alfalfa Dehydrating*, 417 U.S. 134, respondent incurred

no bond discount as a result of its substitution of debentures for preferred stock because the debentures were the equitable equivalent of the claims of the preferred shareholders.

As we show below, the issues petitioner raises do not independently warrant further review.

1. Although petitioner supports the decision below that petitioner incurred discount upon the issuance of its debentures for its outstanding preferred stock, it urges (Pet. 7-14) that the court of appeals erred because it understated the amount of discount arising out of the transaction. It variously characterizes its claim as a "loss" incurred upon the repurchase of some of its debentures for cash in 1954 (Pet. 7-8), or as a somewhat lesser claim for amortizable bond discount, *i.e.*, interest, for 1953 and 1954 (Pet. 12-13). Petitioner principally argues that the court of appeals should have separately considered its claim that it incurred a loss on the transaction (see Pet. App. A 2a, n. 2; Pet. App. E 68a, 75a, 76a).[1]

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[1]The judgment of the court of appeals was entered on December 13, 1974. The government's petition for rehearing, with a suggestion for rehearing *en banc*, was denied on February 4, 1975. Petitioner did not file a petition for rehearing in the court of appeals and filed its petition for a writ of certiorari on May 2, 1975, more than 90 days after the entry of judgment by the court of appeals. Thus, if the government's petition for rehearing did not extend petitioner's time for filing a petition for a writ of certiorari, this Court has no jurisdiction to consider the petition. See 28 U.S.C. 2101(c).

While it is settled that a timely petition for rehearing tolls the running of the time within which the petitioner for rehearing may file a petition for a writ of certiorari, *United States* v. *Healy*, 376 U.S. 75, 78, this Court has never squarely held that a petition for rehearing by one party extend the time of another party to file a petition for a writ of certiorari. However, in *Communist Party of Indiana* v. *Whitcomb*, 414 U.S. 441, 444-446, the Court held that a motion for reconsideration filed by the appellee in the district court suspended the finality of that court's judgment and thereby extended the time within which the appellant could file a notice of appeal to this Court. Since the court of appeals entered a single judgment in this case, it would appear that the government's petition for rehearing suspended its finality, so that this petition for a writ of certiorari was timely.

There was no occasion for the court of appeals to address separately petitioner's loss argument. As the Court observed in *Commissioner* v. *National Alfalfa Dehydrating, supra,* 417 U.S. at 145, any possible ambiguity in the interest-loss approach with respect to bond discount disappears once it is recognized that original issue discount is compensation for the use of money, *i.e.,* interest. See *United States* v. *Midland-Ross Corp.,* 381 U.S. 54, 57, 66.

Moreover, petitioner's loss claim, which it made only for 1954, is barred by the statute of limitations. The pertinent facts with respect to this issue are as follows. In March 1962, the Commissioner of Internal Revenue assessed additional income taxes of $736,596.63 against petitioner for 1953. Petitioner paid this assessment on March 28, 1962. In November 1962, the Commissioner assessed additional income taxes of $783,271.95 for 1954. Petitioner paid this assessment on or about December 3, 1962. On March 24, 1964, petitioner filed claims for refund for 1953 and 1954, asserting for the first time that its debentures had been issued at a discount, measured by the difference between the face amount of the debentures and the fair market value of the preferred and preference shares for which they were exchanged (R. A5-A9).[2]

On or about February 10, 1966, petitioner filed what it characterized as an amended and supplemental claim for refund for 1954, based for the first time upon the amount for which its preferred shares had been issued,

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[2]"R." refers to the joint appendix filed in the court of appeals.

and asserting further that it was entitled to a deduction for a loss measured by the difference between the amount received upon issuance of its stock and the amount paid in retirement of debentures exchanged for that stock. In the alternative, it claimed a larger deduction for bond discount, measured by the difference between the face amount of debentures and the amount originally received upon issuance of the preferred shares. After six months had elapsed and the Commissioner had not acted upon the 1953 claim and had denied the 1954 claim, petitioner instituted this suit for refund, making alternative claims for loss and amortizable bond discount deductions (Pet. App. E 75a-76a; R. A8, A26-A27).

Section 6511(a) of the Internal Revenue Code of 1954 provides that a claim for refund must be filed within three years from the time the return was filed or two years from the time the tax was paid, whichever period expires later. Section 6511(b)(1) states that no refund shall be allowed unless the taxpayer filed his claim within the prescribed period. Here, petitioner's amended claim for 1954 was filed in February 1966, more than two years after it paid the tax in December 1962 (Pet. App. E 75a). It is therefore barred by the statute of limitations in Section 6511(a). *Jones* v. *Liberty Glass Co.*, 332 U.S. 524; *Real Estate Title Co.* v. *United States*, 309 U.S. 13, 17-18.

The fact that petitioner's loss claim was made in an untimely amendment of its original timely claim does not cure this defect, for this Court has squarely held that the untimely amendment of a claim for refund does not permit recovery upon new facts and a different ground. *United States* v. *Andrews*, 302 U.S. 517. Indeed, if the rule were otherwise, a taxpayer could continue to amend a claim for refund indefinitely so as to postpone its final disposition by the Commissioner.

2. Assuming *arguendo* that petitioner's loss claim for 1954 is not barred by the statute of limitations, petitioner did not incur a deductible loss for that year upon the repurchase of some of its outstanding debentures which had been issued in exchange for its preferred stock. The Code does not permit a corporation to claim a deductible loss if it issues stock, amasses large amounts of earnings and profits, and then retires some or all of the issued stock at the enhanced value resulting from its profitable history. Yet that is the substance of petitioner's loss claim, *i.e.*, that after years of large profits, it paid out more with respect to its preferred shares than it received upon their issuance.

Sections 311, 336, and 1032 of the 1954 Code provide that a corporation shall recognize neither gain nor loss upon distribution of property with respect to its stock or upon issuance of its stock for property. Although those provisions were made explicit for the first time in the 1954 Code, they represented no change in the law. See S. Rep. No. 1622, 83d Cong., 2d Sess., pp. 247, 258, 426 (1954). Prior to 1954, as this Court had occasion to point out (*United States* v. *Anderson, Clayton & Co.*, 350 U.S. 55, 57-59; *Helvering* v. *Reynolds Co.*, 306 U.S. 110, 114-115), the Treasury Regulations had long provided, with exceptions not here relevant, that corporations realized no income upon issuance or retirement of their shares of stock.

Petitioner would have suffered no loss, deductible or otherwise, when it retired its preferred shares for cash at stated value, accrued and unpaid dividends, and call premiums, regardless of the amount for which they had earlier been issued. Accordingly, it suffered no loss when it retired, at less than face amount, its obligations to pay those amounts, which it had issued upon retirement of its preferred shares.

3. Petitioner alternatively argues (Pet. 12-13) that it is entitled to deductions for 1953 and 1954 for amortizable bond discount equal to a ratable portion of the difference between the face amount of the debentures ($115,246,950) and the original consideration it received upon the issuance of its preferred stock ($45,323,846).[3] It contends that the court of appeals erred in holding that the measure of the discount was the smaller amount equal to the difference between the face amount of the debentures ($115,246,950) and their market value at issuance (approximately $106,000,000).

If, as we submit, this Court's *National Alfalfa* decision establishes that petitioner incurred no amortizable bond discount upon the issuance of its debentures, there is no issue in this case relating to the correct measure of discount. There would accordingly be no occasion to review the measure of discount the court of appeals applied, and the petition for a writ of certiorari should be denied.

If, however, the Court deems it appropriate to set for argument the issue of the existence of discount presented by our petition, it would also be appropriate to grant this petition, limited to the aspect of the question presented relating to petitioner's claim for amortizable bond discount.

Respectfully submitted.

ROBERT H. BORK,
Solicitor General.

JULY 1975.

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[3]Petitioner issued its three classes of preferred shares for cash and property having an aggregate fair market value of $45,323,846. However, the stated value of these shares was $58,690,000 (Pet. App. A 5a and n. 5). See also Pet. App. B 43a, n. 2.